MEMORANDUM

To: PSB Docket No. 5980 Service List
Beth Sachs, Vermont Energy Investment Corporation
EEU E-mail Service List

From: James A. Volz, Chairman
David C. Coen, Board Member
John D. Burke, Board Member

Re: Adoption of Revised Avoided Costs

Date: December 5, 2007

In Docket 5980, the Vermont Public Service Board ("Board") approved avoided costs for use in energy efficiency programs run by the Energy Efficiency Utility ("EEU"). We also accepted the parties' proposal (as set out in the Memorandum of Understanding ("MOU") between the Department of Public Service ("DPS" or "Department") and other parties) establishing a process for later revisions of those avoided costs. Specifically, paragraph 11 of the MOU provides (in relevant part) that:

> The DPS also will update avoided costs used in EEU program and measure screening and estimates of economically achievable energy efficiency potential as appropriate. Such updates shall be filed with and approved by the Board after an opportunity for other parties to file written comments and request a technical workshop. The Department intends to perform such updates as part of its core functions to the extent reasonably feasible.[1]

On November 9, 2007, the Department requested that the Board approve updated avoided costs for use in program and measure screening by the EEU. Consistent with the process we adopted in Docket 5980, the Board solicited comments from interested persons and conducted a technical workshop on November 27, 2007, to review the Department's analysis.

[1] Docket 5980, Order of 9/30/99, Appendix A at A-9 (¶ 11).

We have considered the Department's proposal and the parties' statements at the workshop.[2] As we explain below, we find the proposal to be reasonable and accept the Department's recommended avoided costs for use in program and measure screening only.

Avoided Costs

The proposed avoided costs were developed by the Avoided-Energy-Supply-Component ("AESC") Study Group in conjunction with other states in the New England region.[3] As the Department stated at the workshop, the regional group has historically updated these costs biannually and plans to continue this practice. The cost projections that the Department asks us to adopt were customized for Vermont based upon the regional avoided-cost analysis.

The Department recommended that the Board approve updated energy, capacity, and other fossil-fuel avoided costs; the Department did not recommend any changes to the avoided transmission and distribution component, the line-loss multipliers, or the costing-period definitions presently in use for efficiency screening. The Department did not propose to adopt the externality adder for carbon dioxide emissions that is included in the AESC study; rather, the Department proposed that the current environmental adder continue to be used. The Department also did not propose to adopt the DRIPE (Demand Reduction Induced Price Effects) adjustment shown in the AESC study, although it states that it will continue to work with the AESC Study Group to refine the DRIPE concept.

No party filed written comments on the Department's proposal. Attendees at the workshop asked questions about the AESC study that was the basis for the proposed avoided costs, but did not raise any objections to the adoption of the new avoided costs.

We accept the Department's recommendation and adopt the avoided energy and capacity costs, as well as the end-use avoided costs for natural gas and other fuels. (A copy of these avoided capacity and energy costs is attached. The avoided natural gas costs are located on pages 2-39, 2-40 and Appendix B-14 of the AESC report. The costs for other fossil fuels are contained on page 4-8 and in Exhibit F-2 of the AESC report.)

At this time, we do not adopt the DRIPE adjustment or the carbon dioxide externality adder contained in the AESC report.

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[2]The Board did not receive any written comments on the Department's proposal.

[3]The AESC study, prepared by Synapse Energy Economics, Inc., is entitled "Avoided Energy Supply Costs in New England: 2007 Final Report " and is available on the Department's web site at: http://publicservice.vermont.gov/pub/aescstudy.html.

Future Revisions to Avoided Costs

The Department states that, in the future, it expects to update avoided costs every two years, coinciding with the production of new analyses by the AESC Study Group. This appears to be a reasonable interval for reconsidering avoided costs.

There are two issues we would like the Department to address the next time it reviews avoided costs — (1) whether it is appropriate for Vermont Gas and the EEU to use the same natural-gas avoided costs; and (2) whether the current environmental adder should be changed.

At the workshop, representatives from Vermont Gas and Efficiency Vermont stated that they do not currently use the same avoided natural-gas costs. Given that Vermont Gas and the EEU provide service to the same customers, it is unclear to us why it is appropriate for them to use different avoided natural-gas costs. We are particularly concerned that it could be confusing to customers if the cost-effectiveness of possible energy efficiency measures differs, depending on which entity performs the analysis. We are pleased that, at the workshop, representatives from Vermont Gas, Efficiency Vermont, and the Department stated that they would discuss this issue. We encourage them to include the City of Burlington Electric Department in those discussions.

We understand and agree with the Department's decision not to propose changes to the current environmental adder at the present time. However, given the length of time since this adder has been reviewed and the recent implementation of the Regional Greenhouse Gas Initiative, we believe reconsideration of the current environmental adder should occur as part of the next review of avoided costs.

We recognize that the reconsideration of the environmental adder may well be contentious (whether or not the Department recommends that the adder be changed). As a result, we encourage the Department to allow sufficient time between the filing of its recommendation and the desired implementation date of the new avoided costs for the Board to establish a reasonable schedule for resolution of this issue.